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In the Supreme Court of the United States

OCTOBER TERM, 1962

No. 96

UNITED STATES, PETITIONER

v.

BUFFALO SAVINGS BANK

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF NEW YORK

REPLY BRIEF FOR THE UNITED STATES

The government's position in this case rests upon three basic propositions of federal law underlying the decision of *United States* v. *New Britain*, 347 U.S. 81: (1) that perfected federal and State tax liens are of equal dignity; (2) that their priority is determined by application of the rule of first in time, first in right; and (3) that State law cannot impair the priority of the federal tax lien. The application of these propositions to the facts of this case, requiring reversal of the decision below, is not dislodged by any of the arguments advanced either by the Buffalo Savings Bank or by the *amicus curiae*, the American Bar Association. The Bank argues that the *New Britain* decision can be distinguished; the *amicus*

urges that *New Britain* be reconsidered and overruled, but, taken together, their arguments serve only to emphasize that *New Britain* was rightly decided on the basis of fundamental principles of law, and is controlling here.

I

THE *NEW BRITAIN* CASE CANNOT BE DISTINGUISHED AND IS CONTROLLING HERE

The brief of Buffalo Savings Bank, like the opinion below, rests primarily upon the contention that *New Britain* is distinguishable.[1] Most of the arguments advanced by the Bank were anticipated and answered in the government's main brief. Here, we briefly summarize the Bank's arguments and our answers.

1. The Bank first asserts (Br. 6–8) that under New York law the taxpayer-mortgagor's property interest in the mortgaged property—to which the federal lien attached—is diminished by the mortgagee's right to have local real estate taxes and assessments be first paid as "expenses" of any foreclosure sale. As the government pointed out in its main brief (pp. 15–17), this is not so. Under New York law, the mortgagor is the owner of the fee, subject only to the mortgage; and, as this Court said in *United States* v. *Brosnan*, 363 U.S. 237, 241, the property interest of the mortgagor to which the federal lien can attach is not di-

[1] The Bank recognizes (Br. 25, fn. 2) that an argument that the Court in *Aquilino* v. *United States*, 363 U.S. 509, and *United States* v. *Durham Lumber Co.*, 363 U.S. 522, recognized the right of a State by statute to make the ownership rights of a taxpayer in real property subject to diminution by annual real estate taxes so that the federal lien attaches only to the diminished ownership "would, of course, amount to a refutation of the New Britain doctrine."

minished by the particular means of enforcement possessed by a prior mortgagee.

2. The Bank attempts (Br. 8–12) to distinguish *New Britain* on two grounds. First, it argues that the mortgagee was not a party to the *New Britain* case, so that the problem of circuity of liens and the mortgagee's rights under the recordation statute (Section 3672 of the 1939 Code; now Section 6323 of the 1954 Code) was not presented. A review of the briefs in that case is sufficient to refute the Bank's argument. They show that the parties presented extensive arguments addressed to the point that under the rule of "first in time, first in right" local taxes would be paid from the share of the mortgagee to whom Congress had granted priority in Section 3672. Thus, the government stated in its opening brief in *New Britain* (Br. 17):

> Full effect would be given to the federal statute by setting aside funds sufficient to pay the mortgages and judgment (covered by Section 3672) before satisfying the federal liens. Connecticut could then satisfy the municipal liens (excluded from Section 3672) from the sum so set apart. This procedure, suggested by the Government and referred to by this Court in *Spokane County* v. *United States*, 279 U.S. 80, 91—and adopted in *Samms* v. *Chicago Title & Trust Co.*, 111 N.E. 2d 172 (Ill. App.)—is the only one by which both the federal and the state law are given effect to the fullest permissible extent. If the end result be deemed incongruous in that the State takes from mortgagee and judgment creditor part or all of what the Federal Government leaves with them, the

> "incongruity arises by virtue of [the] state law and not by virtue of the federal enactment." *Samms* v. *Chicago Title & Trust Co.*, *supra*, at 176. The State is free, of course, to subordinate the liens of its municipality in situations of this kind and rank them last on the ground that they fall behind the federal liens which yield in turn to the mortgages and judgment. The State is not free, however, unless Congress grants a further exception thus far withheld, to protect its City's liens at the expense of the paramount federal liens.

Thereafter, the City of New Britain filed a supplemental brief and the United States, a reply brief, which were devoted primarily to a consideration of this very issue (see Supplemental Brief for Respondent, City of New Britain, pp. T2–T3, T4, N1; Reply Brief for the United States, pp. 1–10).[2] As stated in our main brief (pp. 26–27), this Court was thus fully informed in *New Britain* that its decision required the mortgagee, who was accorded priority by the federal law, to bear the burden of the later arising local taxes when it held that the mortgagee would only be entitled to recover as against the federal tax lien "the amount necessary to pay the mortgage."

The Bank also argues (Br. 11): "In Connecticut the real estate taxes and assessments are paid because

[2] Under the circumstances, there is no basis for the bank's contention (Br. 9–10) that "[i]t was not until the case went back to the Superior Court of Hartford County, on remand from this Court, as Brown vs. General Laundry Service, Inc., 19 Conn. Sup. 335, 113 A. 2d 601, that the question of 'circular priority' entered the case to reduce the amount previously set aside for the judgment creditor, William G. Dunn, in order to pay in full the federal tax lien."

they are liens on the mortgaged property, while in New York they are paid as expenses of the foreclosure sale." As the government pointed out in Point B-2 of its main brief (pp. 18–22), a State cannot by the choice of a label subordinate a federal tax lien to any later arising state-created lien.

3. The Bank errs in contending (Br. 13–15) that the *Brosnan* case supports the decision below on the theory that the Pennsylvania foreclosure proceedings there involved resulted not only in divesting the property of the junior federal lien, but also in paying fully the later-arising local tax liens. The *Brosnan* decision does not deal with or decide the latter issue. As we stated in our main brief (pp. 22–25), the only question presented in *Brosnan* was whether a mortgagee could divest the property of junior federal tax liens by procedures other than those outlined in the federal statute (28 U.S.C. 2410). The United States contended that it could not and asserted that despite the State-authorized foreclosure it still retained a lien on the real property or at least a right of redemption. The decision rejected the government's contentions and held that procedures authorized by State law for the foreclosure of senior liens and the divestiture of all junior liens could be recognized without impairing the priority of the federal tax lien (363 U.S. at 250–252). The *Brosnan* decision thus relates solely to the procedures whereby a senior lienor may divest the real property of a junior federal lien. The federal government never presented and the decision in no way determined the issue for which it is cited by petitioner—whether proceeds of the foreclosure sale

over and above those necessary to satisfy the senior lien could lawfully be used to satisfy later-arising tax claims of the State prior to those of the federal government which had priority under federal law.[5]

4. The Bank's fourth contention (Br. 15–17) is that under the government's concession in *Crest Finance Co. v. United States*, 368 U.S. 347, that a mortgage lien on property is not rendered inchoate because the value of the security is uncertain, "it follows that there can be no objection in this case to the fact that the mortgagor's equity in the mortgaged premises varies in value, by decreasing as real estate taxes and assessments are levied against the mortgaged property, pursuant to an established tax rate, after the filing of the federal lien." This conclusion of the Bank is a *non sequitur* and rests upon a misinterpretation of the government's position in *Crest Finance*. In *Crest*, the prior lien was in a definite amount, fixed before the federal tax lien arose, and the property to which the lien attached was fixed and certain; the government conceded only that the necessity for final ascertainment of the value of this property subject to the lien[6] did not affect its choateness.

[5] The Bank overemphasizes (Br. 14) the quoted excerpt from the government's brief in *Brosnan*. The government was there simply explaining one of the consequences that might result if Section 2410 procedures were not held to be exclusive. Whether the consequence would have been upheld as consistent with federal tax lien priorities was an issue left by the government for litigation in another case.

[6] The lien attached to moneys due under the terms of a specific contract for work already performed in delivering truckloads of fill. By the time the tax assessments were made, the taxpayer had completed performance of the contract and all

The government expressly distinguished the case of *United States* v. *Ball Construction Co.*, 335 U.S. 587, where this Court held that a prior lien could not be extended to include future, contingent claims, which is exactly the character of the later arising local real estate tax liens here involved. (Cf. government's main brief, p. 21.)

5. The Bank also urges (Br. 17–27) that it was the intention of Congress, as evidenced by its enactment of Section 3672(a) of the Internal Revenue Code of 1939 (now Section 6323(a) of the 1954 Code) and 28 U.S.C. 2410, to protect the "mortgagee," not only as to the principal indebtedness, but also as to any disbursements necessary for the protection or preservation of the mortgage lien. This contention, as already noted (*supra*, pp. 3–4), was rejected by *New Britain*. See 347 U.S. 81, 88. The Bank adds nothing to the arguments advanced on this issue in *New Britain* other than the dissenting opinion of Judge Haynsworth in *United States* v. *Bond*, 279 F. 2d 837 (C.A. 4), cer-

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that remained to be done was the final computation of the precise amount due. This was to be based upon an engineering measurement of the compacted fill instead of a measurement based on the number of truckloads delivered, on which weekly estimates had been based. The United States conceded that this final computation of the value of the security (from an estimated figure based on truckloads to a precise figure based on the engineering measurement of the compacted fill) did not render the lien of Crest inchoate when it was specific and definite in three essential respects: (1) the identity of the lienholder (Crest Finance); (2) the amount of the lien; and (3) the property to which it attached (the accounts receivable for the work already performed under the specific contract). See Memorandum for the United States in *Crest Finance Co., Inc.* v. *United States*, *supra*, at 5.

tiorari denied, 364 U.S. 895. The decision of this Court in *United States* v. *Union Central Life Ins. Co.*, 368 U.S. 291, decided subsequent to *Bond*, fully discusses the legislative history of the recordation provision, and holds that the sole purpose of that provision was to protect mortgagees (as well as pledgees, purchasers and judgment creditors) from secret government liens. To accomplish this, it provided that in order to be "valid" against such claimants, the federal tax lien had to be recorded. Nothing in the statute or its legislative history suggests that Congress undertook to define the nature and extent of a mortgagee's interest in property, or to alter the fundamental rules of priority of federal and competing liens in any other respect. In short, Section 3672 merely added the requirement of recordation to the federal tax lien. It added nothing to the mortgage lien.

II

THE *NEW BRITAIN* CASE WAS CORRECTLY DECIDED AND SHOULD BE REAFFIRMED

The American Bar Association, in its *amicus curiae* brief, urges this Court to reconsider and overrule the *New Britain* decision. It concedes that affirmance of the decision below would require overruling *New Britain*.

1. The first ground upon which re-examination is urged is the claim that a State tax lien is inherently superior to a federal tax lien, and that the *New Britain* decision "fails to recognize the essential difference between real property taxes and federal taxes generally" (Amicus Brief, p. 9). While the govern-

ment has answered this argument in its main brief (pp. 13–15), we point out additionally that acceptance of this argument would necessitate overruling not merely *New Britain*, but also *Michigan* v. *United States*, 317 U.S. 338; *Spokane County* v. *United States*, 279 U.S. 80; *New York* v. *Maclay*, 288 U.S. 290; *United States* v. *Texas*, 314 U.S. 480; and *Illinois* v. *Campbell*, 329 U.S. 362, which directly uphold the supremacy of the federal tax lien against the priority accorded by a State law to its tax liens. It is, in short, a contention that federal law must yield to State law in the field of lien priorities. The long-settled answer of this Court is well stated in *Michigan* v. *United States*, *supra*, where the State of Michigan claimed priority for its real estate tax liens over the unrecorded lien of the United States for estate taxes which arose at the date of death (317 U.S. at 340–341):

> We do not stop to inquire whether this construction of the state statutes is the correct one, for we think the argument ignores the effect of a lien for federal taxes under the supremacy clause of the Constitution. The establishment of a tax lien by Congress is an exercise of its constitutional power "to lay and collect taxes." Article I, § 8 of the Constitution. *United States* v. *Snyder*, 149 U.S. 210. And laws of Congress enacted pursuant to the Constitution are by Article VI of the Constitution declared to be "the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."

"It is of the very nature and essence of a lien, that no matter into whose hands the property goes, it passes *cum onere*." *Burton* v. *Smith*, 13 Pet. 464, 483; *Rankin* v. *Scott*, 12 Wheat. 177, 179; *Howard* v. *Railway Co.*, 101 U.S. 837, 845. Hence it is not debatable that a tax lien imposed by a law of Congress, as we have held the present lien is imposed, cannot, without the consent of Congress, be displaced by later liens imposed by authority of any state law or judicial decision. *United States* v. *Snyder*, *supra*; *United States* v. *Greenville*, 118 F. 2d 963. Similarly we held that the priority of payment commanded by R. S. § 3466 could not be set aside by state legislation. *United States* v. *Texas*, 314 U.S. 480, 486; *Spokane County* v. *United States*, 279 U.S. 80; *New York* v. *Maclay*, 288 U.S. 290; cf. *Missouri* v. *Ross*, 299 U.S. 72.

As the federal lien with which we are here concerned attached to private property prior to the acquisition of any interest in that property by the state, we need not consider the extent to which Congress may give, or intended by § 315(a) to give, priority to a federal lien over a previously perfected state lien. Compare *New York* v. *Maclay*, *supra*, 292; *Spokane County* v. *United States*, *supra*, 95; *United States* v. *Texas*, *supra*, 484–486.

2. We have already answered (*supra*, pp. 3–4, 7–8) the Bar Association's contention (pp. 11–19) that the interests of the mortgagee were not considered in *New Britain* and that the prior mortgagee is deprived of the protection intended by Congress by virtue of the provisions of Section 3672(a) of the 1939 Code if

the subsequent property taxes must be paid from its share of the proceeds of sale of the mortgaged property. The "bizarre" results described by the *amicus* brief (pp. 12–13) are in substance no more than the inevitable consequences of the different rules of priority established by federal and State law. The federal rule with respect to its tax liens is a strict rule of first in time, first in right; the State rule accords tax liens, and other State-created liens, exceptional priority.[8] The *amicus* brief would resolve the problem by denying the supremacy which federal law gives to federal liens.[9]

3. Finally, the *amicus* presents the view (Br. 19–21) of "[s]ome lawyers" of the American Bar Association that the entire issue of priorities is a matter of state property law. This Court, however, has re-

[8] The argument that the federal tax lien should be subordinated to everything which is ahead of the mortgage would not only subject the federal tax lien to other State preferred liens, such as landlord's and mechanic's liens, but is logically fallacious. One might "just as well start at any point on the circle—*e.g.*, by contending that the United States, being ahead of the property tax, is ahead of everything that is inferior to the property tax, including the pre-existing mortgage." Plumb and Wright, *Federal Tax Liens* (July 1961), p. 78.

[9] The problem of so-called circuity of liens, arising in non-federal contexts, is an old one, for which there is no perfect solution. Osborne on *Mortgages* (1951), Sec. 209, pp. 532–539; IV *American Law of Property*, Sec. 17.33, pp. 627–629; *Circuity of Liens—A Proposed Solution*, 38 Col. L. Rev. 1267 (1938); Campbell, *Protection Against Indirect Attack*, *Harvard Legal Essays*, pp. 3, 16–20. The solutions depend upon the legal relationships of the parties in each particular case. In meeting this problem, the Court of Appeals of the State of New York has adopted a rule similar to the *New Britain* rule. *Bacon* v. *Van Schoonhoven*, 89 Hun 158, affirmed, 87 N.Y. 446.

peatedly rejected this view and held that the relative priority of a federal tax lien is a question of federal, not State, law—a view which the Court recently reiterated in *Aquilino* v. *United States*, 363 U.S. 509, 512–514.

Respectfully submitted.

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NOVEMBER 1962.

Both *Aquilino* and *United States* v. *Bonham Lumber Co.*, 363 U.S. 522, turned on the question whether, as a matter of State law, the respective taxpayers had property interests in the funds to which the federal government had laid claim. Contrary to the suggestion of the *amicus* (Br. 21), State law was not applied to determine priorities.

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